

ORIGINAL



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MEMORANDUM

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TO: Docket Control

FROM: Ernest G. Johnson
Director
Utilities Division

EA for EGJ

DATE: October 12, 2007

RE: STAFF REPORT FOR ICR WATER USERS ASSOCIATION, INC.;
APPLICATION FOR AUTHORIZATION TO ASSUME NEW DEBT
(DOCKET NO. W-02824A-07-0139)

Attached is the Staff Report for ICR Water Users Association, Inc.'s application for authorization to assume new debt to fund capital improvements and repairs. Staff recommends partial approval of the request.

EGJ:SPI:red

Originator: Steve Irvine

Attachment: Original and sixteen copies

Arizona Corporation Commission
DOCKETED
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DOCKET CONTROL

Service List for: ICR Water Users Association, Inc.
Docket No. W-02824A-07-0139

Mr. Robert M. Busch
ICR Water Users Association, Inc.
P.O. Box 5669
Chino Valley, Arizona 86323

Mr. Robert Metli, Esq.
Ms. Marcie Montgomery, Esq.
Snell & Wilmer L.L.P.
One Arizona Center
Phoenix, Arizona 85004-2202

Mr. Christopher C. Kempley
Chief Counsel, Legal Division
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

Mr. Ernest G. Johnson
Director, Utilities Division
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

Ms. Lyn Farmer
Chief Administrative Law Judge, Hearing Division
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

**STAFF REPORT
UTILITIES DIVISION
ARIZONA CORPORATION COMMISSION**

**ICR WATER USERS ASSOCIATION, INC.
DOCKET NO. W-02824A-07-0139**

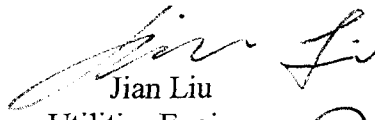
APPLICATION FOR APPROVAL OF DEBT

OCTOBER 12, 2007

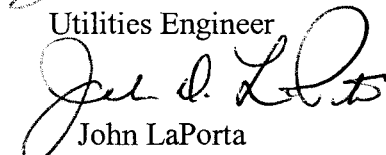
STAFF ACKNOWLEDGMENT

The Staff Report for ICR Water Users Association, Inc., Docket No. W-02824A-07-0139 is the responsibility of the Staff members listed below. Steve Irvine is responsible for the financial review and analysis. Jian Liu is responsible for the engineering analysis. John LaPorta is responsible for the customer service memorandum.

Steve Irvine
Public Utilities Analyst IV



Jian Liu
Utilities Engineer



John LaPorta
Public Utility Consumer Analyst

EXECUTIVE SUMMARY
ICR WATER USERS ASSOCIATION, INC.
DOCKET NO. W-02824A-07-0139

ICR Water Users Association, Inc. ("ICR" or "Company") filed an application with the Arizona Corporation Commission ("Commission") on March 6, 2007, requesting authorization of \$100,000 of new debt. On June 26, 2007 ICR filed a rate case application.

ICR is an Arizona non-profit corporation providing water service to customers in Yavapai County, Arizona. As of March 2007 ICR had approximately 396 residential customers, 11 commercial customers, and 7 irrigation customers.

ICR indicates in the application that it has a need to purchase a backup emergency generator and to construct a security fence around a well. The cost of the generator is \$40,000 and the cost of the fencing is approximately \$10,000. With this application ICR seeks authorization to secure a one-year line of credit for \$100,000. ICR plans to make use of the balance of the line of credit for funding of unanticipated capital repairs.

Staff's financial analysis indicates that given a \$50,000 line of credit ICR's TIER ratio is negative 10.22 and the DSC ratio is 1.38. Given a \$100,000 line of credit ICR's TIER ratio is negative 5.11 and the DSC ratio is 0.69. Staff's cash flow analysis indicates an ability to support a \$50,000 line of credit with a residual \$19,872 cash flow.

ICR's pro forma capital structure including a \$50,000 line of credit as well as AIAC and CIAC is 1.0 percent short-term debt, 0.0 percent long-term debt, negative 8.7 percent equity, 79.9 percent AIAC, and 27.7 percent CIAC.

Staff concludes that obtaining a line of credit of \$50,000, not to exceed a term of one year for purposes of acquiring a back up generator and security fencing by ICR is reasonable, is within its corporate powers, is compatible with the public interest, would not impair its ability to provide services and would be consistent with sound financial practices provided that ICR files within its current rate case a plan to increase the percentage of equity in its capital structure.

Staff recommends that the Commission authorize IRC to enter into a line of credit not to exceed \$50,000 for a term of one-year to fund acquisition of a back-up generator and security fence.

Staff recommends that ICR file within its current rate case a plan to increase the percentage of equity in its capital structure.

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Introduction

ICR Water Users Association, Inc. ("ICR" or "Company")¹ filed an application with the Arizona Corporation Commission ("Commission") on March 6, 2007, requesting authorization of \$100,000 of new debt. On June 26, 2007 ICR filed a rate case application.²

Public Notice

On May 1, 2007 ICR filed an affidavit of publication from Prescott Newspapers, Inc. with Docket Control. The affidavit attests that on April 27, 2007 notice of the filing was given in the Courier, a newspaper published in Yavapai County. A copy of the notice is attached.

Background

ICR is an Arizona non-profit corporation providing water service to customers in Yavapai County, Arizona. As of March 2007 ICR had approximately 396 residential customers, 11 commercial customers, and 7 irrigation customers.

Purpose of the Financing Application

ICR asserts in its application that it has a need to purchase a back-up emergency generator and to construct a security fence around a well. The cost of the generator is \$40,000 and the cost of the fencing is approximately \$10,000. With this application ICR seeks authorization to secure a one-year line of credit for \$100,000. ICR plans to make use of the balance of the line of credit for funding of unanticipated capital repairs.

Financial Analysis

TIER and DSC

Staff prepared Schedule SPI-1 using the financial information from Exhibit I of ICR's application. Column A depicts the financial information as of December 31, 2006 and is based on the financial information contained in ICR's application. As ICR currently has no long-term debt the times interest earned ratio ("TIER") and debt service coverage ratio ("DSC") are not meaningful in column A. The pro forma information in column B shows the impact of an addition of a \$50,000 line of credit. The pro forma information in column C shows the impact of an addition of a \$100,000 line of credit. Given a \$50,000 line of credit ICR's TIER ratio is negative 10.22 and the DSC ratio is 1.38. Given a \$100,000 line of credit ICR's TIER ratio is negative 5.11 and the DSC ratio is 0.69.

¹ ICR is an Arizona corporation which was granted a CC&N by the Commission in Decision No. 59263.

² (Docket No. W-02824A-07-0388)

DSC represents the number of times internally generated cash will cover required principal and interest payments on short-term and long-term debt. A DSC greater than 1.0 indicates that operating cash flow is sufficient to cover debt obligations.

TIER represents the number of times earnings will cover interest expense on short-term and long-term debt. A TIER greater than 1.0 means that operating income is greater than interest expense. A TIER less than 1.0 is not sustainable in the long term but does not necessarily mean that debt obligations cannot be met in the short term.

DSC is a better metric than TIER for measuring ICR's ability to support the requested one-year line of credit since DSC measures the ability to meet all obligations. DSC indicates the ICR has the ability to support a \$50,000 line of credit, but not a \$100,000 line of credit.

Cash Flow Analysis

Staff also conducted a cash flow analysis to test the ability of ICR to support a \$50,000 line of credit. The analysis is shown in SPI-2 and indicates an ability to support a \$50,000 line of credit with a \$19,872 residual cash flow.

Capital Structure

ICR's December 31, 2006 capital structure consisted of 0.0 percent short-term debt, 0.0 percent long-term debt, and negative 100.0 percent equity. The pro forma capital structure including a \$50,000 line of credit is 13.5 percent short-term debt, 0.0 percent long-term debt, and negative 113.5 percent equity. The pro forma capital structure including a \$100,000 line of credit is 31.2 percent short-term debt, 0.0 percent long-term debt, and negative 131.2 percent equity. This information is portrayed in Schedule SPI-1. The negative equity position has negative implications for issuing debt and should be remedied in the foreseeable future. In the pro forma example the line of credit is depicted as short-term debt as ICR proposes a year-long line of credit.

Capital Structure including AIAC and CIAC

ICR's capital structure inclusive of Advances-in-Aid-of-Construction ("AIAC") and Contributions-in-Aid-of-Construction ("CIAC") is portrayed in Schedule SPI-1. ICR's 2006 capital structure in this example is 0.0 percent short-term debt, 0.0 percent long-term debt, negative 8.8 percent equity, and 80.7 percent AIAC, and 28.0 percent CIAC.

ICR's pro forma capital structure including the proposed year-long \$50,000 line of credit as well as AIAC and CIAC is 1.0 percent short-term debt, 0.0 percent long-term debt, negative 8.7 percent equity, 79.9 percent AIAC, and 27.7 percent CIAC. Staff typically recommends that water companies with access to capital markets maintain a minimum of 40 percent equity in their capital structure to reduce financial risk. Staff typically recommends that water companies that have no access to capital markets should minimize to the extent possible the presence of debt in

their capital structure. Staff typically recommends that a non-profit corporation maintain at least 30 percent equity in its capital structure. Non-profit corporations should contain funding from debt and AIAC sources to moderate levels in order to reduce financial risk since they lack access to the equity capital markets.

Engineering Analysis

Staff's Engineering Report is attached. Staff reviewed the material cost estimates of the proposed plant improvements. Staff concludes that ICR's \$50,000 cost estimate for the proposed generator and fence appears reasonable. Staff makes no "used and useful" determination of the proposed plant and no particular future treatment should be inferred for rate-making or rate base purposes.

Compliance

ICR has no outstanding Commission compliance issues.

Conclusion and Recommendations

Staff concludes that obtaining of a line of credit of \$50,000 not to exceed a term of one year for purposes of acquiring a back up generator and security fencing by ICR is reasonable, is within its corporate powers, is compatible with the public interest, would not impair its ability to provide services and would be consistent with sound financial practices provided that ICR files within its current rate case a plan to increase the percentage of equity in its capital structure.

Staff concludes that given ICR's present financial condition it is imprudent for ICR to enter into a line of credit for an additional \$50,000 for unanticipated repairs.

Staff recommends that the Commission authorize ICR to enter into a line of credit not to exceed \$50,000 or a term of one-year to fund acquisition of a back-up generator and security fence.

Staff recommends that ICR file within its current rate case (Docket No. W-02824A-07-0388) a plan to increase the percentage of equity in its capital structure.

Staff further recommends authorizing ICR to engage in any transaction and to execute any documents necessary to effectuate the authorizations granted.

Staff further recommends the Company file with Docket Control, as a compliance item in this docket, copies of documents evidencing execution of the transaction(s) within 60 days of execution.

FINANCIAL ANALYSIS

Selected Financial Data Including Immediate Effects of the Proposed Debt

	[A] <u>12/31/2006</u>		[B] <i>Pro Forma</i> <u>\$50,000 LOC</u>		[C] <i>Pro Forma</i> <u>\$100,000 LOC</u>	
1 Operating Income	\$	(24,543)	\$	(24,543)	\$	(24,543)
2 Depreciation & Amort.		96,817		96,817		96,817
3 Income Tax Expense		0		0		0
4						
5 Interest Expense		0		2,401		4,803
6 Repayment of Principal				50,000		100,000
7						
8						
9 TIER						
10 [1+3] ÷ [5]		N/M		-10.22		-5.11
11 DSC						
12 [1+2+3] ÷ [5+6]		N/M		1.38		0.69
13						
14						
15						
16						
17 <i>Capital Structure:</i>						
18 Short-term Debt	\$151	0.0%	\$50,000	13.5%	\$100,000	31.2%
19						
20 Long-term Debt	\$0	0.0%	\$0	0.0%	\$0	0.0%
21						
22 Common Equity	(\$420,856)	-100.0%	(\$420,856)	-113.5%	(\$420,856)	-131.2%
23						
24 Total Capital	<u>(\$420,705)</u>	<u>-100.1%</u>	<u>(\$370,856)</u>	<u>-100.0%</u>	<u>(\$320,856)</u>	<u>-100.0%</u>
25						
26						
27 <i>Capital Structure Inclusive of AIAC and CIAC:</i>						
28 Short-term Debt	\$151	0.0%	\$50,000	1.0%	\$100,000	2.0%
29						
30 Long-term Debt	\$0	0.0%	\$0	0.0%	\$0	0.0%
31						
32 Common Equity	(\$420,856)	-8.8%	(\$420,856)	-8.7%	(\$420,856)	-8.6%
33						
34 AIAC	\$3,872,698	80.7%	\$3,872,698	79.9%	\$3,872,698	79.1%
35						
36 CIAC	\$1,344,539	28.0%	\$1,344,539	27.7%	\$1,344,539	27.5%
37						
38 Total Capital	<u>\$4,796,532</u>	<u>100.0%</u>	<u>\$4,846,381</u>	<u>100.0%</u>	<u>\$4,896,381</u>	<u>100.0%</u>
39						
40						

CASH FLOW ANALYSIS


Year End 2006

Based on Financials Provided in Application

Line No.		
1	Operating Revenue:	\$ 270,797
2	Operating Expenses:	
3	All Other Operating Expenses	\$ 195,684
4	Depreciation	96,817
5	Property Taxes	2,795
6	Other taxes	45
7	Total Operating Expense	\$ 295,341
8	Operating Income (Line 1 - Line 7)	(\$24,544)
9	Add back Depreciation Expense	\$96,817
10	Less refunds of Advances	\$0
11	Total Cash Available	\$72,273
	Less Existing Debt Service on Loan Balance:	
12	Annual Principal and Interest Payment (\$0 x 12)	\$0
13	Annual Debt Service Reserve Payment (\$0 x 12)	\$0
14	Subtotal	\$0
	Less Debt Service on Proposed Loan:	
15	Annual Principal and Interest Payment	\$52,401
16	Subtotal	\$52,401
17	Net Cash Flow (Line 11 - Line 14 - Line 16)	\$19,872

M E M O R A N D U M

TO: Steve Irvine
Public Utilities Analyst III
Utilities Division

FROM: John La Porta 
Public Utilities ~~Analyst~~ Consumer Analyst I
Utilities Division

DATE: March 14, 2007

RE: ICR Water Users Association – (W-02824A-07-0139)

On March 6, 2007 ICR Water Users Association (“ICR Water”) filed an application for authorization to assume new debt.

After researching the Consumer Services database from January 1, 2004 through March 13, 2007 there have been zero complaints, inquiries and opinions filed against ICR Water.


Corporations Division reports ICR Water is in good standing.

If I can be of any further assistance, please feel free to call me.

MEMORANDUM

DATE: August 28, 2007

TO: Steve Irvine
Public Utilities Analyst IV
Utilities Division

FROM: Jian W. Liu 
Utilities Engineer
Utilities Division

RE: ICR Water Users Association, Inc.
Docket No. W-02824A-07-0139 (Financing)

Introduction

ICR Water Users Association, Inc. ("Company" OR "ICR") presently provides utility service to approximately 375 water customers in portions of Yavapai County, Arizona. ICR is an Arizona non-profit corporation, and the member-customers elect a board of directors who manage and operate the Company according to its by-laws. The ICR's principal business office is located at 246 N Highway 89, Suite A, Chino Valley, Arizona 86323.

Financing Application

On March 6, 2007, the Company filed an application with the Arizona Corporation Commission ("Commission") requesting authority to assume new debt in the form of a line of credit in the total amount of \$100,000.

Engineering Analysis

On June 26, 2007, the Company filed an application with the Commission for determination of the current fair value of its utility plant and property and for increases in its rates and charges for utility services. Because the Company's water infrastructure is aging, the Company has a current need to make capital improvements and repairs and anticipates making such improvements prior to new rates going into effect.

Within the next six months, the Company anticipates the need to purchase a backup emergency generator as well as construct security fencing around one of its wells.

The Company states that the backup emergency generator is necessary to protect the Company's water supply in the event of a power failure. Presently, there is no backup electricity at the well-site, and any electricity interruption causes the well pumps to shutdown. ICR plans to place a security fence around the well-site with gate and lock since there are numerous developments under construction in the area near the well-site.

Staff concludes that a backup emergency generator and construct security fencing around one of its wells are appropriate.

Cost Analysis

The Company's estimated cost for the proposed backup emergency generator and construct security fence is as follows:

	Costs
100-150 kW generator	\$40,000
Construct security fence	\$10,000

Total: \$50,000

Staff has reviewed the Company's estimates and concludes that they are reasonable. However, no "used and useful" determination of the proposed plant was made, and no particular future treatment should be inferred for rate making or rate base purposes.

Compliance

Arizona Department of Environmental Quality (ADEQ) Compliance

ICR acknowledges that its water systems are NOT currently in compliance with ADEQ reporting requirements for lead and copper and Maximum Residual Disinfection Levels. The Company is working with ADEQ to bring the water systems into full compliance with ADEQ regulations.

Arizona Corporation Commission (ACC) Compliance

According to the Utilities Division Compliance Section, the Company has no delinquent compliance issues with the ACC.

Conclusion

Staff concludes that the plant additions and their associated costs are reasonable and appropriate. However, no "used and useful" determination of the proposed plant was made, and no particular future treatment should be inferred for rate making or rate base purposes.

AFFIDAVIT OF PUBLICATION

STATE OF ARIZONA)
County of Yavapai) ss.

I, **Deseree Zurcher**, being first duly sworn on her oath says:
That she is the **Legal Clerk** of **PRESCOTT NEWSPAPERS, INC.**, an Arizona corporation, which owns and publishes the **COURIER**, a Daily Newspaper published in the City of Prescott, County of Yavapai that the notice attached hereto, namely,

ICR Water Users Association, Inc.
Notice of Application for Authority to Borrow Money
Docket No. W-028A-07-0139

has, to the personal knowledge of affidavit, been published in the news paper aforesaid, according to law, on **27 day of April, 2007** to **27 day of April, 2007** both inclusive without change, interruption or omission, amounting in all 1 insertions, made on the following dates:
April 27, 2007

By: *Deseree Zurcher*
Dated this 27 Day of April, 2007

By: *Michael J Knowlton*
Notary Public

My commission expires:



**NOTICE OF APPLICATION OF
ICR WATER USERS ASSOCIATION, INC.
FOR AUTHORITY TO BORROW MONEY
(DOCKET NO. W-02824A-07-0139)**
On March 6, 2007, ICR Water Users Association, Inc. ("Applicant") filed an application ("Application") with the Arizona Corporation Commission ("Commission") in Docket No. W-02824A-07-0139 for authority to borrow \$100,000 from the National Bank of Arizona to finance capital improvements and repairs within the Applicant's service territory. The Commission may act on the Application with or without a hearing. The Application is available for inspection during regular business hours at the Commission's offices at 1209 West Washington Street, Phoenix, Arizona 85007, or at the offices of the Applicant, 846 N. Hwy 89, Suite A, Chino Valley, AZ 86323.
Intervention in the Commission's proceedings on the Application shall be permitted to any person entitled by law to intervene and having a direct and substantial interest in this matter. Persons desiring to intervene must file a Motion to Intervene with the Commission which must be served upon Applicant and which, at a minimum, shall contain the following information:
1. The name, address and telephone number of the proposed intervenor and of any person upon whom service of documents is to be made if different than the intervenor;
2. A short statement of the proposed intervenor's interest in the proceeding;
3. Whether the proposed intervenor desires a formal evidentiary hearing on the Application and the reasons for such a hearing; and
4. A statement certifying that a copy of the Motion to Intervene has been mailed to Applicant.
The granting of Motions to Intervene shall be governed by A.A.C. R14-3-105, except that all Motions to Intervene must be filed on, or before, the 15th day after this notice.
If you have any questions about this Application, or want further information on intervention, you may contact the Consumer Services Section of the Commission at 1209 West Washington Street, Phoenix, Arizona 85007, or call 1-800-222-7000.
TIC Pub April 27, 2007 Ad 11439